

Financial Audit of the

STATE OF HAWAII

DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES

STATE MOTOR POOL REVOLVING FUND

July 1, 2004 to June 30, 2005

## TABLE OF CONTENTS

	<u>Page</u>
<b>PART I - TRANSMITTAL</b>	1
<b>PART II – MANAGEMENT’S DISCUSSION AND ANALYSIS</b>	3
<b>PART III – FINANCIAL SECTION:</b>	
Independent auditors’ report	7
Financial statements	
Statement of Net Assets	9
Statement of Revenues, Expense and Changes in Net Assets	10
Statement of Cash Flows	11
Notes to Financial Statements	13
<b>PART IV – INTERNAL CONTROL AND COMPLIANCE SECTION:</b>	
Report on Internal Control Over Financial Reporting and on Compliance and other matters Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i>	21
<b>PART V - SCHEDULE OF AUDIT FINDINGS AND QUESTIONED COSTS</b>	23
<b>PART VI - CORRECTIVE ACTION PLAN</b>	24

**PART I**  
**TRANSMITTAL**

November 15, 2005

Comptroller  
State of Hawaii  
Department of Accounting and General Services  
1151 Punchbowl Street  
Honolulu, Hawaii 96813

We have completed our financial audit of State of Hawaii, Department of Accounting and General Services, State Motor Pool Revolving Fund (the "Fund") as of and for the year ended June 30, 2005. The audit was performed in accordance with our agreement with the Fund dated June 25, 2004.

### OBJECTIVES

The primary purpose of our audit was to form an opinion on the fairness of the presentation of the Fund's financial statements as of and for the fiscal year ended June 30, 2005. More specifically, the objectives of our audit were as follows:

1. To provide a basis for an opinion on the fairness of the financial statements of the Fund.
2. To ascertain whether or not expenditures have been made and all revenues and other receipts to which the Fund is entitled have been collected and accounted for in accordance with the laws, rules and regulations, and policies and procedures of the State of Hawaii and the federal government.
3. To ascertain the adequacy of the financial and other management information reports in providing officials at the different levels of the State and the Fund the proper information to plan, evaluate, control and correct program activities.
4. To evaluate the adequacy, effectiveness and efficiency of the systems and procedures for financial accounting, operational and internal controls, and to recommend improvements to such systems and procedures.

## SCOPE OF THE AUDIT

Our audit was performed in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The scope of our audit included an examination of the transactions and accounting records of the Fund for the fiscal year ended June 30, 2005.

## ORGANIZATION OF THE REPORT

This report is organized into six parts:

PART I - presents the transmittal letter.

PART II - presents management's discussion and analysis.

PART III - presents the financial section which includes the Fund's financial statements and the auditors' report on such statements.

PART IV - contains the reports on internal controls and compliance.

PART V - presents the schedule of audit findings and questioned costs.

PART VI - contains the corrective action plan.

At this time, we wish to thank the Fund's personnel for their cooperation and assistance extended to us. We will be happy to respond to any questions that you may have on this report.

Very truly yours,

Michael Y. Ichikawa  
Principal

**COPY**  
**Original document signed by**  
**Egami & Ichikawa CPAs, Inc.**

## **PART II**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS**

## MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the annual financial report presents an analysis of the Fund's financial performance during the fiscal year ending June 30, 2005. Please read it in conjunction with the financial statements which follow this section.

### FINANCIAL HIGHLIGHTS

- The Fund's net assets decreased by 19.06% or \$846,000 in 2005 over 2004. This decrease is mainly because \$1,000,000 of the Fund was transferred out to the State's General Fund.
- The Fund's operating revenues increased by 1.02% or \$21,000 in 2005 over 2004, because of an increase in the motor vehicle repairs revenue.
- The Fund's net nonoperating revenue decreased by 115.38% or \$75,000 in 2005 over 2004 because of a decrease in interest income of \$10,000 and an increase on a loss on disposition of capital assets of \$65,000.

### OVERVIEW OF ANNUAL REPORT

This annual report consists of six parts: Transmittal letter; management's discussion and analysis; financial statements and notes to the financial statements; the report on internal control over financial reporting and compliance; the schedule of audit findings and questioned costs; and the corrective action plan.

### REQUIRED FINANCIAL STATEMENTS

The Financial Statements of the Fund present information about the Fund as a whole and its activities and uses the accrual basis of accounting. The accrual basis which is similar to the accounting basis used by private sector companies recognizes revenues and expenses regardless of when cash is paid or received.

The Statement of Net Assets provides both short-term and long-term information about the Fund's financial position, which reflects the fund's economic condition at the end of the year.

The Statement of Net Assets provides, over time, indicators of the Fund's financial position. The Statement of Net Assets includes all the Fund's assets and liabilities, and provides information about the nature and the amounts of investment in resources (assets) and obligations (liabilities) of the Fund.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

### REQUIRED FINANCIAL STATEMENTS (Continued)

The Statement of Revenues, Expenses and Changes in Net Assets reflect the Fund's current year's revenues and expenses regardless of when cash is received or paid.

The Statement of Cash Flows reflects the flow of cash of the Fund in four categories or activities: operating, investing, capital, and noncapital.

Tables 1 and 2 present a comparative view of net assets and changes in net assets as of June 30, 2005 and 2004.

**TABLE 1**  
**NET ASSETS**  
(Rounded to nearest \$1,000)

	<u>2005</u>	<u>2004</u>
ASSETS:		
Current	\$ 1,398,000	\$ 2,108,000
Capital assets, net of depreciation	<u>2,433,000</u>	<u>2,507,000</u>
Total assets	<u>3,831,000</u>	<u>4,615,000</u>
LIABILITIES:		
Current	138,000	88,000
Long-term	<u>101,000</u>	<u>89,000</u>
Total liabilities	<u>239,000</u>	<u>177,000</u>
NET ASSETS:		
Invested in capital assets, net of related debt	2,433,000	2,507,000
Unrestricted	<u>1,159,000</u>	<u>1,931,000</u>
Total net assets	<u>3,592,000</u>	<u>4,438,000</u>
Total liabilities and net assets	<u>\$ 3,831,000</u>	<u>\$ 4,615,000</u>

Net assets of the Fund decreased by 19.06% in 2005. Investment in capital assets (e.g., vehicles, shop equipment, furniture and fixtures), net of the related debt used to purchase the assets represents a large portion of the funds net assets; \$2,433,000 or 67.73% in 2005 and \$2,507,000 or 56.49% in 2004. Capital assets are used to provide vehicles for state agencies. The Fund's investment in its capital assets is reported net of debt. The resources needed to repay this debt must be provided by other sources, since the capital assets, mainly the vehicles, cannot be used to liquidate the debt. The remaining unreserved assets may be used to finance day to day operations without any constraints established by debt, or other legal requirements.



MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

**TABLE 2**  
**CHANGES IN NET ASSETS**  
(Rounded to nearest \$1,000)

	<u>2005</u>	<u>2004</u>
<b>OPERATING REVENUES</b>		
Motor vehicle rentals	\$ 1,692,000	\$ 1,828,000
Motor vehicle repairs	<u>381,000</u>	<u>224,000</u>
<b>TOTAL OPERATING REVENUES</b>	<u>2,073,000</u>	<u>2,052,000</u>
<b>OPERATING EXPENSES</b>		
General operating and administrative	1,228,000	1,179,000
Depreciation	<u>681,000</u>	<u>628,000</u>
<b>TOTAL OPERATING EXPENSES</b>	<u>1,909,000</u>	<u>1,807,000</u>
<b>INCOME FROM OPERATIONS</b>	164,000	245,000
<b>NET NON OPERATING (EXPENSE) REVENUE</b>	(10,000)	65,000
<b>OPERATING TRANSFERS – GENERAL FUND</b>	<u>(1,000,000)</u>	<u>(929,000)</u>
<b>CHANGE IN NET ASSETS</b>	<u>\$ (846,000)</u>	<u>\$ (619,000)</u>

The Fund's vehicle rental rates are established under the jurisdiction of the Comptroller, as Chief of the Department of Accounting and General Services or the Comptroller's designated representative, the division head of the automotive management division. The increase in operating revenues of 1.02% or \$21,000 in 2005 was primarily due to the increase in motor vehicle repairs.

The increase in general operating expenses of 4.16% or \$49,000 in 2005 was primarily due to increases in fuel costs and repairs during the current year.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

### CAPITAL ASSET AND DEBT ADMINISTRATION

#### Capital Assets

The Fund's investment in capital assets amounted to \$2,433,000 and \$2,507,000 (net of accumulated depreciation of \$2,349,000 in 2005 and \$2,260,000 in 2004). Capital assets include vehicles, shop equipment, furniture, and fixtures.

	<u>2005</u>	<u>2004</u>
ASSETS:		
Capital assets, net of accumulated depreciation:		
Vehicles	\$ 2,419,000	\$ 2,491,000
Shop equipment, furniture and fixtures	<u>14,000</u>	<u>16,000</u>
TOTAL CAPITAL ASSETS, NET	<u>\$ 2,433,000</u>	<u>\$ 2,507,000</u>

#### Debt Administration

There was no debt as of June 30, 2005 and 2004.

**PART III**  
**FINANCIAL SECTION**

## INDEPENDENT AUDITORS' REPORT

Comptroller  
State of Hawaii  
Department of Accounting and General Services  
1151 Punchbowl Street  
Honolulu, Hawaii 96813

We have audited the accompanying financial statements of the State of Hawaii, Department of Accounting and General Services, State Motor Pool Revolving Fund (the "Fund") as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Fund and do not purport to, and do not, present fairly the financial position of the State of Hawaii, or any other segment thereof, as of June 30, 2005, and the changes in its financial position and cash flows, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Fund as of June 30, 2005, and the changes in financial position and cash flows thereof and for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 15, 2005, on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in conjunction with this report in considering the results of our audit.

The management's discussion and analysis on pages 3 – 6, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

This report is intended solely for the information and use of the management of the Fund, the Department of Accounting and General Services and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

Honolulu, Hawaii  
November 15, 2005

**COPY**

**Original document signed by  
Egami & Ichikawa CPAs, Inc.**

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
STATEMENT OF NET ASSETS  
June 30, 2005

CURRENT ASSETS	
Cash in State Treasury	\$ 1,035,923
Motor vehicle rental receivable, net	293,683
Due from other funds	54,706
Inventories	13,606
TOTAL CURRENT ASSETS	<u>1,397,918</u>
NONCURRENT ASSETS	
Capital assets, at cost, less accumulated depreciation	<u>2,433,307</u>
TOTAL ASSETS	<u><u>\$ 3,831,225</u></u>
CURRENT LIABILITIES	
Accounts payable	\$ 95,863
Accrued liabilities	42,299
TOTAL CURRENT LIABILITIES	<u>138,162</u>
NONCURRENT LIABILITIES	
Accrued liabilities	<u>100,419</u>
TOTAL NONCURRENT LIABILITIES	<u>100,419</u>
TOTAL LIABILITIES	<u>238,581</u>
NET ASSETS	
Invested in capital assets, net of related debt	2,433,307
Unreserved	<u>1,159,337</u>
TOTAL NET ASSETS	<u>3,592,644</u>
TOTAL LIABILITIES AND NET ASSETS	<u><u>\$ 3,831,225</u></u>

See accompanying notes to financial statements.

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS  
YEAR ENDED JUNE 30, 2005

OPERATING REVENUES	
Motor vehicle rentals	\$ 1,691,733
Motor vehicle repairs	380,805
TOTAL OPERATING REVENUES	<u>2,072,538</u>
OPERATING EXPENSES	
Depreciation	681,076
Personnel services	574,153
Gas and oil	340,419
Repairs and maintenance	155,462
Special assessment	44,787
Others	112,596
TOTAL OPERATING EXPENSES	<u>1,908,493</u>
INCOME FROM OPERATIONS	<u>164,045</u>
NONOPERATING REVENUES (EXPENSES)	
Interest and miscellaneous income	38,070
Loss on disposition of capital assets	(47,830)
TOTAL NONOPERATING REVENUES (EXPENSES)	<u>(9,760)</u>
INCOME BEFORE TRANSFERS	154,285
OPERATING TRANSFER, NET	
General Fund	(1,000,000)
	<u>(1,000,000)</u>
CHANGE IN NET ASSETS	(845,715)
TOTAL NET ASSETS, BEGINNING OF THE YEAR	4,438,359
TOTAL NET ASSETS, END OF THE YEAR	<u>\$ 3,592,644</u>

See accompanying notes to financial statements.

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
STATEMENT OF CASH FLOWS  
YEAR ENDED JUNE 30, 2005

CASH FLOWS FROM OPERATING ACTIVITIES

Receipts from motor vehicle rentals	\$ 1,604,371
Receipts from motor vehicle repairs	380,805
Payments for personnel services	(563,951)
Payments for gas and oil	(340,419)
Payments for repairs and maintenance	(155,462)
Payments for special assessment	(99,420)
Other administrative payments	(61,288)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>764,636</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Interest from pooled funds	<u>38,070</u>
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>38,070</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

Acquisition of capital assets	(786,878)
Proceeds from disposal of equipment	<u>131,759</u>
NET CASH USED IN CAPITAL AND RELATED FINANCING ACTIVITIES	<u>(655,119)</u>

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

Operating transfer out to general fund	<u>(1,000,000)</u>
NET CASH USED IN NONCAPITAL FINANCING ACTIVITIES	<u>(1,000,000)</u>

NET DECREASE IN CASH	(852,413)
----------------------	-----------

CASH, BEGINNING OF THE YEAR	1,888,336
CASH, END OF THE YEAR	<u><u>\$ 1,035,923</u></u>

See accompanying notes to financial statements.



STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
STATEMENT OF CASH FLOWS  
YEAR ENDED JUNE 30, 2005

RECONCILIATION OF LOSS FROM OPERATIONS TO NET  
CASH PROVIDED BY OPERATING ACTIVITIES:

Income from operations	\$ 164,045
Adjustments to reconcile loss from operations to net cash provided by operating activities:	
Depreciation	681,076
(Increase) decrease in assets:	
Motor vehicle rental receivable	(141,994)
Increase (decrease) in liabilities:	
Accounts payable	51,307
Accrued wages payables	3,741
Accrued vacation payables	6,461
	<u>600,591</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 764,636</u>

See accompanying notes to financial statements.

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The State Motor Pool Revolving Fund (the "Fund") was established pursuant to Act 77, Session Laws of Hawaii 1963 (Section 26-6 of the Hawaii Revised Statutes). The Fund is responsible for providing safe and economical transportation for the personnel of state departments and agencies requiring the use of passenger vehicles in connection with official state business. All monies collected are used for the acquisition, operation, repair, maintenance, storage, and disposition of all state-owned vehicles assigned to the State Motor Pool.

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for State and Local Governments through its pronouncements (Statements and Interpretations). Governments are required to follow the pronouncements of the Financial Accounting Standards Board (FASB) issued through November 30, 1989 (when applicable) that do not conflict with or contradict GASB pronouncement. The more significant accounting policies established by GAAP and used by the Fund are discussed below.

Basis of Accounting - The Fund is an internal service fund (proprietary fund type) as defined by the Governmental Accounting Standards Board (GASB), which uses the flow of economic resources measurement focus and accrual basis of accounting as generally applied to commercial enterprises. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Reporting entity - The financial statements reflect only the Fund's financial activities. The State Comptroller maintains the central accounts for all state funds and publishes financial statements for the State of Hawaii (State) annually, which include the Fund's financial activities.

Use of Estimates - The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
NOTES TO THE FINANCIAL STATEMENTS (Continued)  
JUNE 30, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Cash and Cash Equivalents - Cash and cash equivalents are held in the State Treasury. The Director of Finance is responsible for the safekeeping of all monies deposited into the State Treasury (cash pool). The Hawaii Revised Statutes (HRS) authorizes the Director of Finance to invest in obligations of or guaranteed by the U. S. Government, obligations of the State of Hawaii (State), federally-insured savings and checking accounts, time certificates of deposit and repurchase agreements with federally-insured financial institutions. Deposits not covered by federal deposit insurance are fully collateralized by government securities held in the name of the State by third party custodians.

The Director of Finance pools and invests any monies of the Fund, which in the Director's judgment, are in excess of the amounts necessary for meeting the specific requirements of the Fund. Investment earnings are allocated to the Fund based on its equity interest in the pooled monies. For purposes of the financial statements, the Fund considers all cash held in the State Treasury and investments with a maturity of three months or less when purchased to be cash equivalents.

Inventories - Inventories principally supplies are stated at the lower of cost or market with cost being determined by the first-in, first-out method (FIFO).

Capital Assets - Capital assets are defined by the Fund as vehicles, shop equipment, furniture and fixtures with estimated useful lives greater than one year and acquisition costs greater than the following amounts:

Vehicles	\$5,000
Shop equipment, furniture and fixtures	5,000

Capital assets are stated at cost. Donated assets are recorded at their fair market value at the date of donation. Transfers are recorded at cost, net of the depreciation which would have been charged had the asset been directly acquired by the Fund. The cost of normal maintenance and repairs that do not add to the value or materially extend useful lives are charged to operations as incurred. When capital assets are disposed, the cost and related accumulated depreciation are removed from the respective accounts with the resulting gain or loss reflected in operations.

Depreciation is computed under the straight-line method over estimated useful lives as follows:

	<u>Useful Lives</u>
Vehicles	10 years
Shop equipment, furniture and fixtures	5 – 7 years

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
NOTES TO THE FINANCIAL STATEMENTS (Continued)  
JUNE 30, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accumulated Vacation and Sick Leave - The Fund's employees, with certain exceptions, earn vacation leave at the rate of one and three-quarters working days for each month of service. Vacation days may be accumulated to a maximum of ninety days. When termination of employment takes place, the employees are paid their vacation allowance in a lump sum. The Fund records all vacation pay at current salary rates, including additional amounts for certain salary-related payments associated with the payment of compensated absences, in accordance with GASB Statement No. 16, *Accounting for Compensated Absences*. Sick leave is not convertible to pay upon termination of employment and is recorded as an expenditure when taken.

2. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2005, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Vehicles	\$ 4,694,945	\$ 786,878	\$ 771,386	\$ 4,710,437
Shop equipment, furniture & fixtures	<u>71,658</u>	<u>-</u>	<u>-</u>	<u>71,658</u>
Total capital assets	<u>4,766,603</u>	<u>786,878</u>	<u>771,386</u>	<u>4,782,095</u>
Less accumulated depreciation for:				
Vehicles	(2,204,101)	(679,076)	(591,798)	(2,291,379)
Shop equipment, furniture & fixtures	<u>(55,408)</u>	<u>(2,000)</u>	<u>-</u>	<u>(57,408)</u>
Total accumulated depreciation	<u>(2,259,509)</u>	<u>(681,076)</u>	<u>(591,798)</u>	<u>(2,348,787)</u>
Total capital assets, net of depreciation	\$ <u>2,507,094</u>	\$ <u>105,802</u>	\$ <u>(179,588)</u>	\$ <u>2,433,308</u>

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
NOTES TO THE FINANCIAL STATEMENTS (Continued)  
JUNE 30, 2005

3. ACCRUED LIABILITIES

Accrued liabilities consist of the following:

Accrued vacation payable	\$ 107,835
Accrued wages payable	26,183
Accrued workers' compensation	<u>8,700</u>
	142,718
Less current portion	<u>(42,299)</u>
Total accrued liabilities, net of current portion	<u>\$ 100,419</u>

4. WORKERS' COMPENSATION RESERVE

The Fund is fully self-insured for workers' compensation and disability claims which are expensed when incurred. The Fund pays a portion of wages, medical bills, and judgments as stipulated by the Department of Labor and Industrial Relations, and other costs for injured workers. During the year ended June 30, 2005, there were no payments for workers' compensation claims and disability expenses. The Fund has recorded a reserve of \$8,700 for the expected cost of open reported claims based on historical cost information for closed and open claims as of June 30, 2005.

5. CHANGES IN NON-CURRENT LIABILITIES

Changes in non-current liabilities were as follows:

	Beginning <u>Balance</u>	<u>Increases</u>	<u>Decreases</u>	Ending <u>Balance</u>	Due within <u>one year</u>
Accrued liabilities	\$ <u>132,516</u>	\$ <u>52,080</u>	\$ <u>41,878</u>	\$ <u>142,718</u>	\$ <u>42,299</u>
Total non-current liabilities	\$ <u>132,516</u>	\$ <u>52,080</u>	\$ <u>41,878</u>	\$ <u>142,718</u>	\$ <u>42,299</u>

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
NOTES TO THE FINANCIAL STATEMENTS (Continued)  
JUNE 30, 2005

6. RETIREMENT BENEFITS

Employees' Retirement System

All eligible employees of the Fund are required by HRS Chapter 88 to become members of the Employees' Retirement System of the State of Hawaii (ERS), a cost-sharing multiple-employer public employee retirement plan. The ERS provides retirement benefits as well as death and disability benefits and is governed by a Board of Trustees. All contributions, benefits and eligibility requirements are established by HRS Chapter 88 and can be amended by legislative action. The ERS issues a comprehensive annual financial report that is available to the public. The report may be obtained by writing to the ERS at 201 Merchant Street, Suite 1400, Honolulu, Hawaii 96813.

Prior to June 30, 1984, the plan consisted of only a contributory option. In 1984, legislation was enacted to add a non-contributory option for members of the ERS who are also covered under Social Security. Persons who are employed in positions not covered by Social Security are precluded from the non-contributory option. The non-contributory option provides for reduced benefits and covers most eligible employees hired after June 30, 1984. Employees hired before that date were allowed to continue under the contributory option or to elect the new non-contributory option and receive a refund of employee contributions. All benefits vest after five and ten years of credited service under the contributory and non-contributory options, respectively.

Both options provide a monthly retirement allowance based on the employee's age, years of credited service, and average final compensation (AFC). The AFC is the average salary earned during the five highest paid years of service, including the vacation payment, if the employee became a member prior to January 1, 1971. The AFC for members hired on or after that date is based on the three highest paid years of service, excluding the vacation payment.

Most covered employees of the contributory option are required to contribute 7.8% of their salary. The funding method used to calculate the total employer contribution requirement is the Entry Age Normal Actuarial Cost Method. Under this method, employer contributions to the ERS are comprised of normal cost plus level annual payments required to liquidate the unfunded actuarial liability over the remaining period of 27 years from June 30, 2002.

The State's contribution requirement as of June 30, 2004, 2003 and 2002, based on the most recent information available, was approximately \$181,614,000, \$158,622,000, and \$113,984,000 respectively. The State contributed 100% of its required contributions for those years.

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
NOTES TO THE FINANCIAL STATEMENTS (Continued)  
JUNE 30, 2005

6. RETIREMENT BENEFITS (Continued)

Changes in salary growth assumptions and investment earnings pursuant to Act 100, Session Laws of Hawaii (SLH) 1999, decreased the June 30, 2002 and 2001 required contributions. Act 233, SLH of 2002, increased the 2003 contribution by providing a one-time lump-sum pensioner bonus to retirees who were 70 years and older with at least 20 years of credited service as of June 30, 2002. Also Act 284, SLH of 2001, provided an increase in pension benefits effective 2003 to retirees with military service. The Fund's covered payroll was approximately \$444,627 in 2005. The retirement plan contributions charged to the Fund's operation was \$60,629 in 2005.

Post-Retirement Health Care and Life Insurance Benefits

In addition to providing pension benefits, the State, pursuant to HRS Chapter 87, provides certain health care and life insurance benefits to all qualified employees.

For employees hired before July 1, 1996, the State pays the entire monthly health care premium for employees retiring with ten or more years of credited service, and 50% of the monthly premium for employees retiring with fewer than ten years of credited service.

For employees hired after June 30, 1996, and who retire with fewer than ten years of service, the State makes no contributions. For those retiring with at least ten years but fewer than 15 years of service, the State pays 50% of the retired employees' monthly Medicare or non-Medicare premium. For employees hired after June 30, 1996, and who retire with at least 15 years but fewer than 25 years of service, the State pays 75% of the retired employees' monthly Medicare or non-Medicare premium; for those retiring with over 25 years of service, the State pays the entire health care premium.

Contributions are financed on a pay-as-you-go basis. The Fund's share of the expense for post-retirement benefits for the year ended June 30, 2005 was \$36,927.

Effective July 1, 2003, the Hawaii Employer-Union Health Benefit Trust Fund (EUTF) replaced the Hawaii Public employees Health Fund under Act 88, SLH of 2001. The EUTF was established to provide a single delivery system of health benefits for state and county employees, retirees, and their dependents.

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
NOTES TO THE FINANCIAL STATEMENTS (Continued)  
JUNE 30, 2005

7. COMMITMENTS AND CONTINGENCIES

Accumulated Sick Leave Pay

Sick leave accumulates at the rate of one and three-quarters working days for each month of service without limit, but can be taken only in the event of illness and is not convertible to pay upon termination of employment. However, a state employee who retires or leaves government service in good standing with sixty days or more of unused sick leave is entitled to additional service credit in the ERS. The Fund's accumulated sick leave pay is based on current salary rates, including additional amounts for certain salary-related payments associated with the payment of compensated absences, in accordance with GASB Statement No. 16, *Accounting for Compensated Absences*. As of June 30, 2005, sick leave accumulations were approximately \$277,527.

Deferred Compensation Plan

The State offers its employees a deferred compensation plan (Plan) created in accordance with Internal Revenue Code Section 457. The Plan, available to all state employees, permits employees to defer a portion of their compensation until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

Governmental Accounting Standards Board Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*, which was issued October 1997, requires deferred compensation plans to be reported as an expendable trust if they meet the fiduciary fund criteria defined in National Council on Governmental Accounting Statement 1. The State's deferred compensation plan does not meet those criteria. Accordingly, the assets and liabilities of the deferred compensation plan are not reported in the State's or the Fund's financial statements.

All plan assets are held in a trust fund to protect them from claims of the State's general creditors. The State has no responsibility for investment losses, but does have the duty of due care that would be required of an ordinary prudent investor.



STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
NOTES TO THE FINANCIAL STATEMENTS (Continued)  
JUNE 30, 2005

8. CENTRAL SERVICE AND DEPARTMENTAL ADMINISTRATIVE EXPENSES

HRS Section 36-27 requires that the Fund be assessed its pro rata share of central service expenses of government in relation to other special funds based on a percentage of the Fund's receipts. HRS Section 36-30 requires that the Fund be assessed its pro rata share of administrative expenses incurred by the Department of Accounting and General Services (DAGS), based on the ratio of the general administrative service expenses to DAGS' net departmental expenses. There was no HRS Section 36-27 assessment in 2005. The total of the assessment under HRS Section 36-30 was \$44,787 in 2005.

9. RISK MANAGEMENT

The Fund is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; and workers' compensation. The State generally retains the first \$250,000 per occurrence of property losses and the first \$4 million with respect to general liability claims. Losses in excess of those retention amounts are insured with commercial insurance carriers. The limit per occurrence for property losses is \$100 million except for flood and earthquake which is \$25 million and the annual aggregate for general liability losses per occurrence is \$10 million. The State also has an insurance policy to cover medical malpractice risk in the amount of \$20 million per occurrence and in the aggregate. The State is generally self-insured for workers' compensation and automobile claims.

The estimated reserve for losses and loss adjustment costs includes the accumulation of estimates for losses and claims reported prior to fiscal year-end, estimates (based on projections of historical developments) of claims incurred but not reported, and estimate of costs for investigating and adjusting all incurred and unadjusted claims. Amounts reported are subject to the impact of future changes in economic and social conditions. The State believes that, given the inherent variability in any such estimates, the reserves are within a reasonable and acceptable range of adequacy. Reserves are continually monitored and reviewed, and as settlements are made and reserves adjusted, the differences are reported in current operations. A liability for a claim is established if information indicates that it is probable that a liability has been incurred at the date of the combined financial statements and the amount of the loss is reasonably estimable.

## **PART IV**

### **INTERNAL CONTROL AND COMPLIANCE SECTION**

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON  
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL  
STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING  
STANDARDS*

Comptroller  
State of Hawaii  
Department of Accounting and General Services  
1151 Punchbowl Street  
Honolulu, Hawaii 96813

We have audited the financial statements of the State of Hawaii, Department of Accounting and General Services, State Motor Pool Revolving Fund (the “Fund”) as of and for the year ended June 30, 2005, and have issued our report thereon dated November 15, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the Fund’s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted certain matters that we have reported to management of the Fund, in a separate letter dated November 15, 2005.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, including applicable provisions of the Hawaii Public Procurement Code (Chapter 103D of the Hawaii Revised Statutes) and procurement rules, directives and circulars, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the management of the Fund, the Department of Accounting and General Services and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

Honolulu, Hawaii  
November 15, 2005

**COPY**

**Original document signed by  
Egami & Ichikawa CPAs, Inc.**

**PART V**

**SCHEDULE OF AUDIT FINDINGS AND QUESTIONED COSTS**

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
SCHEDULE OF AUDIT FINDINGS AND QUESTIONED COSTS  
YEAR ENDED JUNE 30, 2005

**SECTION I - SUMMARY OF AUDITORS' RESULTS**

**FINANCIAL STATEMENTS:**

Type of auditors' report issued:	<u>Unqualified</u>
Internal control over financial reporting:	
Material weaknesses identified?	<u>No</u>
Reportable condition identified that is not considered to be material weakness	<u>None reported</u>
Noncompliance material to financial statements noted?	<u>No</u>

**SECTION II - FINANCIAL STATEMENT FINDINGS**

**Status of Prior Year's Comments**

No matters were reported.

**Current Year's Comments**

No matters were reported.

## **PART VI**

### **CORRECTIVE ACTION PLAN**

STATE OF HAWAII  
DEPARTMENT OF ACCOUNTING AND GENERAL SERVICES  
STATE MOTOR POOL REVOLVING FUND  
CORRECTIVE ACTION PLAN  
JUNE 30, 2005

A corrective action plan is not required since there were no audit findings and questioned costs reported for the year ended June 30, 2005.